An introduction to Reserves for small charities

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- Liz Pepler MIAB FRSA
- Director, Embrace Finance
- Charity finance and governance specialist
- Treasurer Trustee, Association of Chairs
- 20 plus years experience of leading and governing charities
- Member of the Institute of Accounting and Bookkeeping
- www.embracefinance.org.uk

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What we talk about when we talk about reserves

1. What the Charity Commission requires
2. Revisiting first principles
3. Operational benefits of reserves
4. How to calculate actual reserves
5. What level of reserves do we need
6. What a good reserves statement looks like
7. Reserves and resilience

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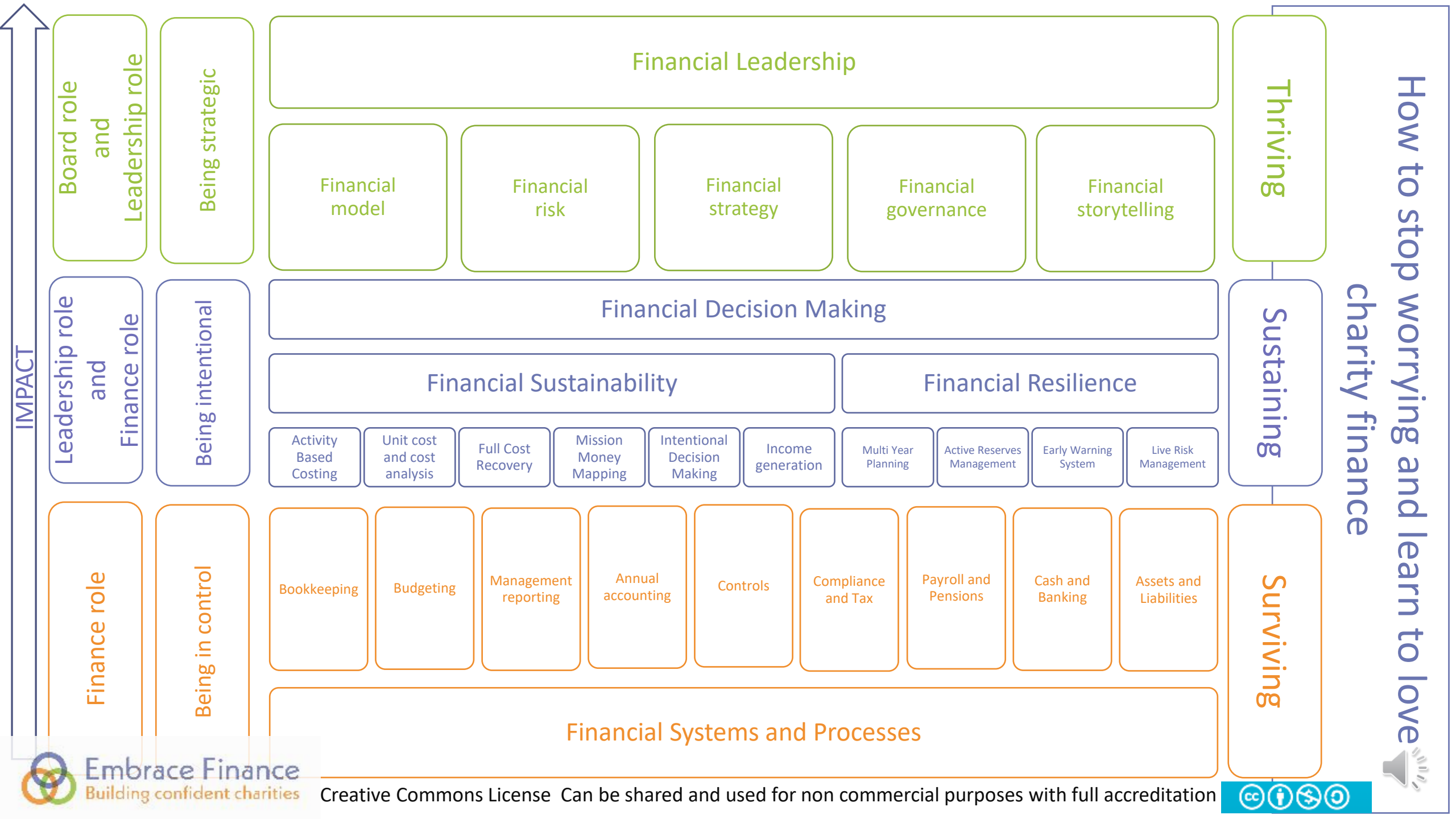

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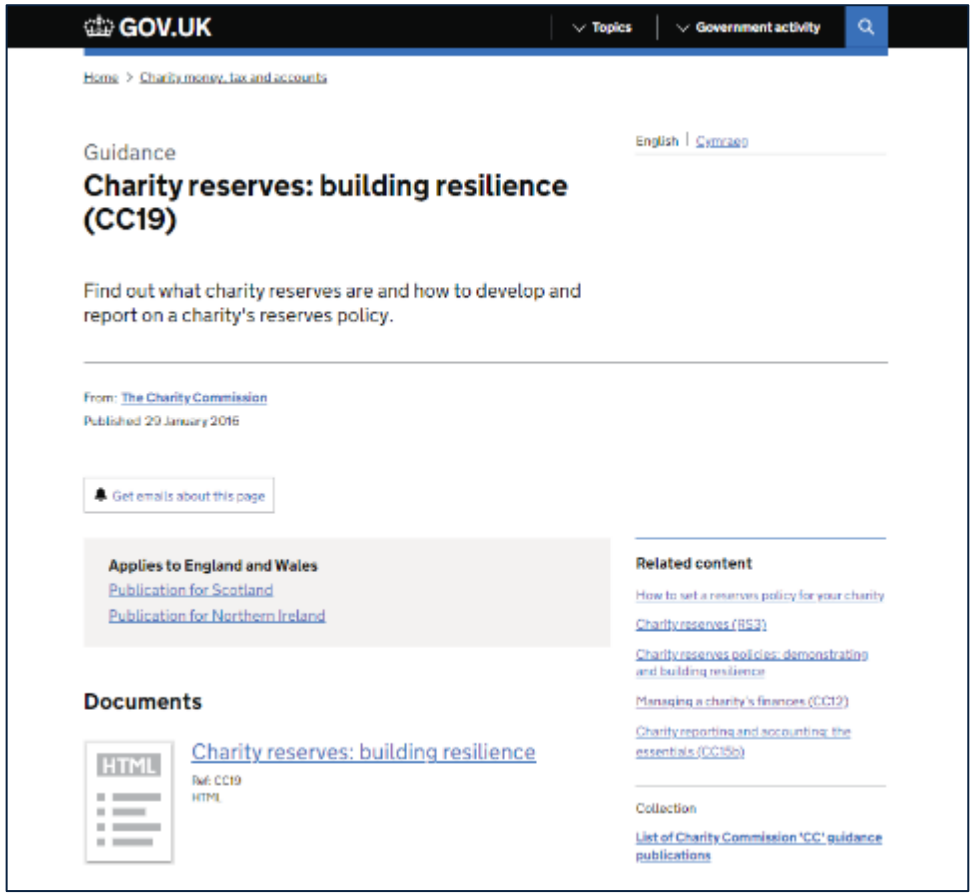
Charity Commission guidance

- CC19 Charity Reserves: building resilience
- There are 167,000 charities on the Charity Commission Register. The guidance is written for all
- It caters for very simple reserves policies for smaller and more simple organisations and for larger, more complex charities
- It's best to revisit the guidance in your own time, and apply those bits that are most appropriate for your own organisation
- This is but a mere introduction



https://www.gov.uk/government/publications/charities-and-reserves-cc19/charities-and-reserves

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CC19 | First principles

- As charities, we are here to spend our resources on our charitable objects for the public benefit
- Trustees need to justify any funds that are not spent
- We do this by adopting a formal reserves policy in accordance with SORP, which we publish in our Trustee's Annual Report and Accounts

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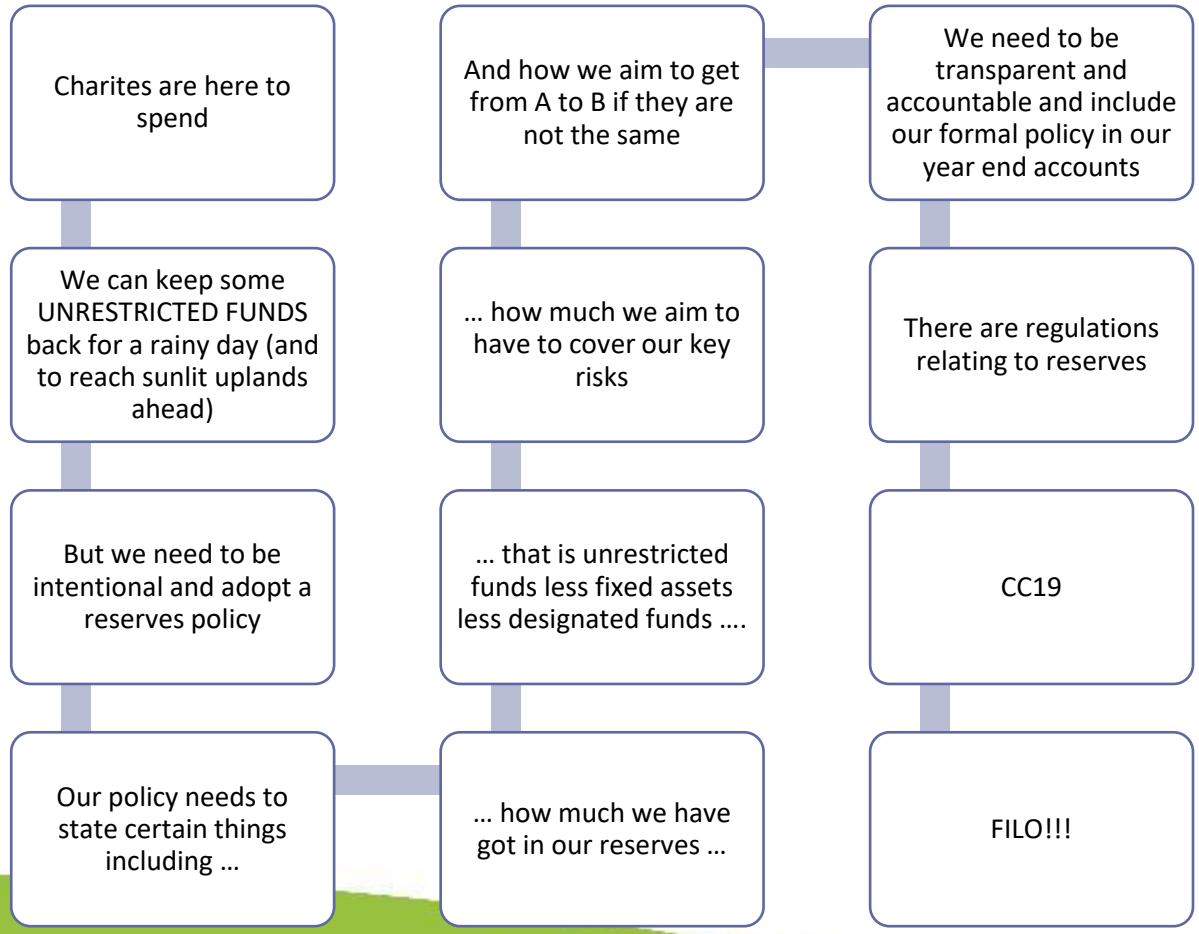
Setting a reserves policy



Source https://www.gov.uk/government/publications/charities-and-reserves-cc19/charities-and-reserves#understanding-reserves-and-the-need-for-a-reserves-policy

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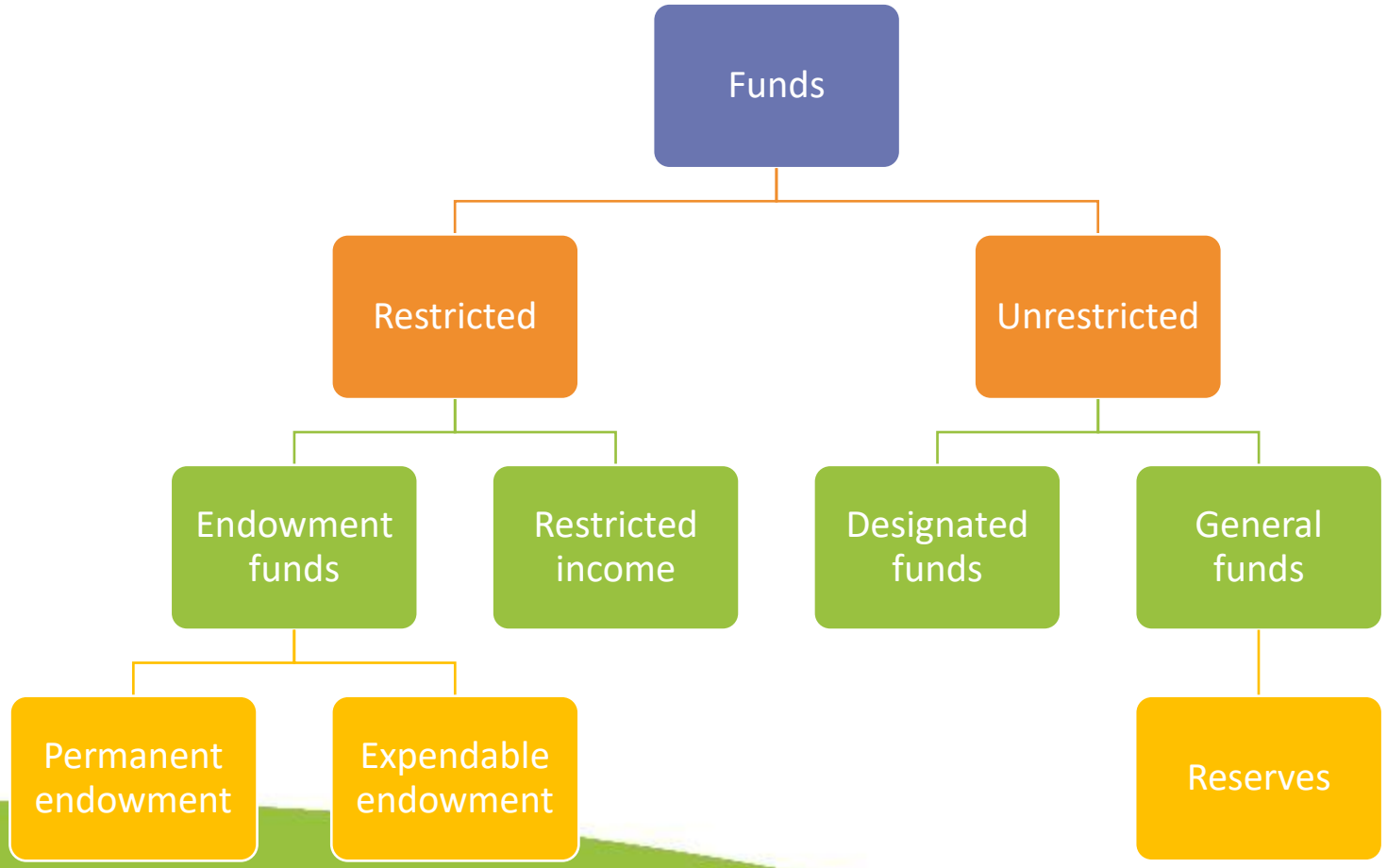
A note about funds



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CC19 | The upsides of managing reserves well

regulatory requirement

give confidence to funders

build financial resilience

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But actually it is about social change

Reserves help us ensure that we can meet the needs of beneficiaries' today, tomorrow, next week, month year and in 10, 20 years time.

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What numbers do we need to know

Calculate our actual level of reserves

Identifying our financial position

Identify our target level of reserves

Identify our financial security

And, if needed, plan how to get from A to B

Map out a financial strategy

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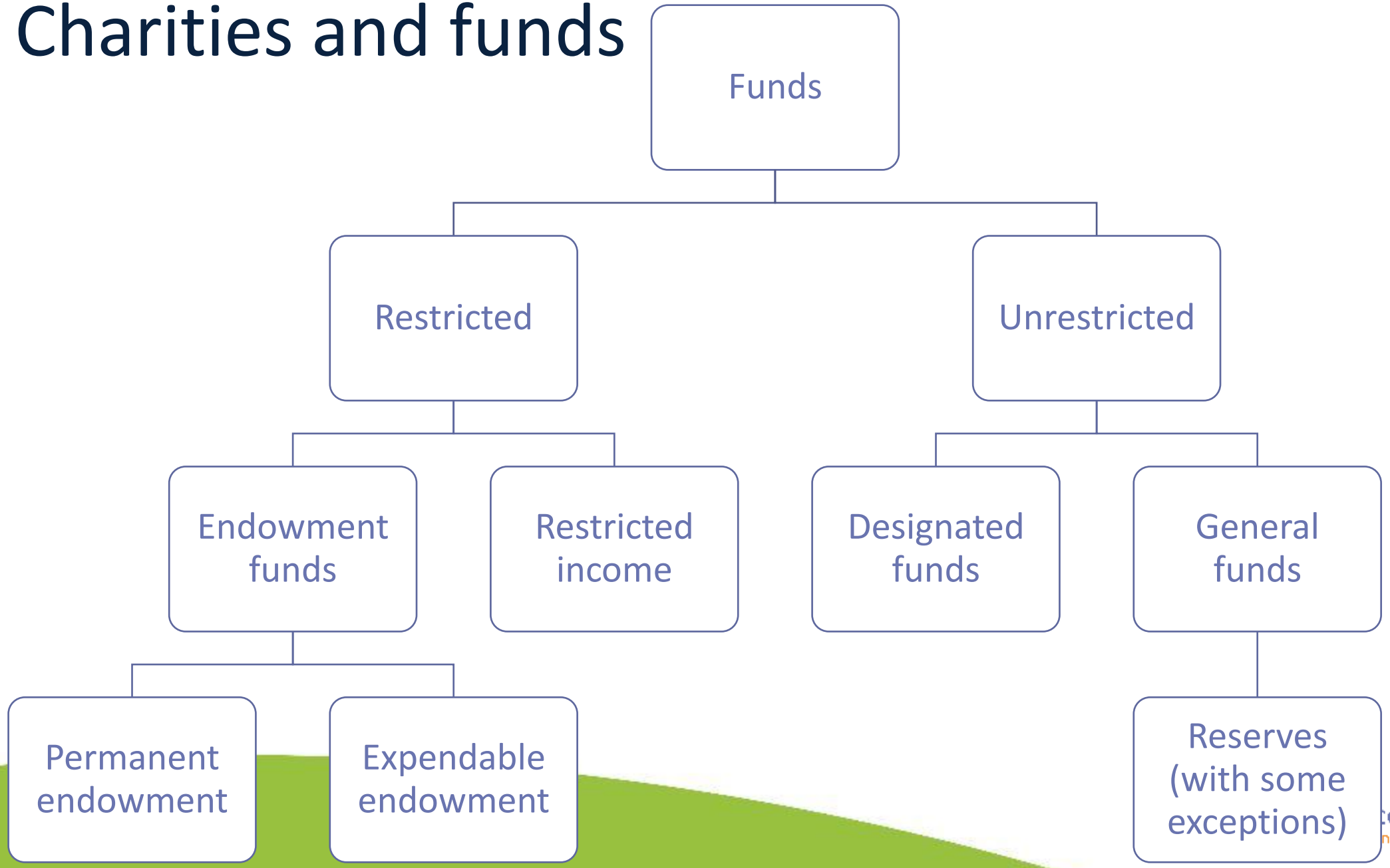
Charities and funds



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How to calculate actual reserves held

Reserves are that part of a charity's unrestricted funds that are freely available to spend on any of the charity's purposes.

Our reserves are our unrestricted funds after we have deducted:

- tangible fixed assets used to carry out the charity's activities, such as land and buildings
- designated funds for essential future spending, e.g. funding a project that can not be met from future income
- programme-related investments those held solely to further the charity's purposes
- commitments that have not been provided for as a liability in the accounts

https://www.gov.uk/government/publications/charities-and-reserves-cc19/charities-and-reserves

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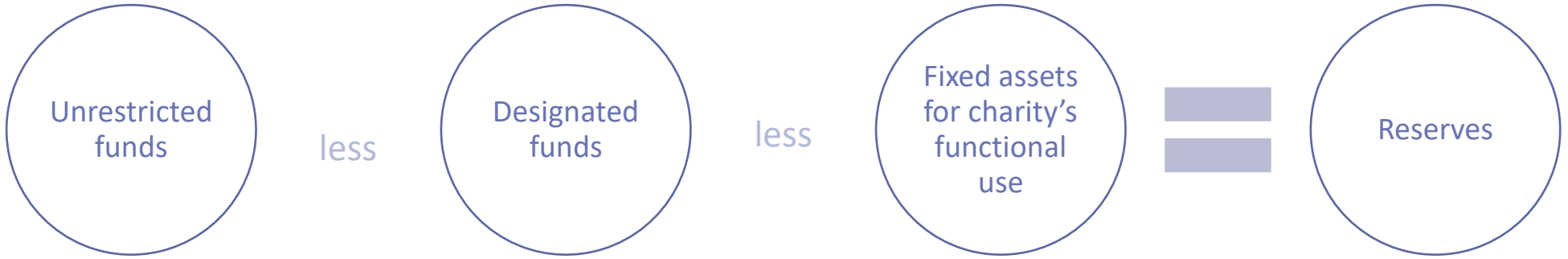
How to calculate actual reserves held



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Reserves | How to calculate actual reserves held

Balance sheet

As at 31 March 2019

Company no. 08287034

	Note	2019 £	2018 £
Fixed assets			
Investments	9	1	1
Current assets			
Debtors	10	13,939	12,621
Cash at bank and in hand		254,623	225,932
		268,562	238,553
Liabilities			
Creditors: amounts falling due within one year	11	(20,989)	(9,583)
Net current assets		247,573	228,970
Net assets		247,574	228,971
The funds of the charity	13		
Restricted funds		104,214	144,262
Unrestricted revenue funds		143,360	84,709
Total charity funds		247,574	228,971

If we were to do this for the very first time we would:

- Look at our balance sheet
- Identify our unrestricted funds
- Deduct fixed assets
- Deduct designated funds
- Deduct other commitments
- Adjust for changes since the balance sheet date

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Reserves | How to calculate our target reserve?

- There is no single level, or even a range of, reserves that is right for all charities.
- Any target reserve level needs to reflect the particular circumstances of the individual charity.
- To do this, trustees need to know the reasons why the charity should hold reserves and the trustees should consider how much should be held to meet them.

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Reserves | How to calculate our target reserve?

We take a risk-based approach based on:

- income and expenditure forecasts, and
- analysis of any future needs

Helpful to note:

‘Trustees who hold (or do not hold) reserves without attempting to relate their need for reserves to factors such as these will have difficulty in satisfactorily explaining why they hold (or do not hold) the level of reserves that they do.’

Charity reserves: building resilience - GOV.UK (www.gov.uk) (abridged)

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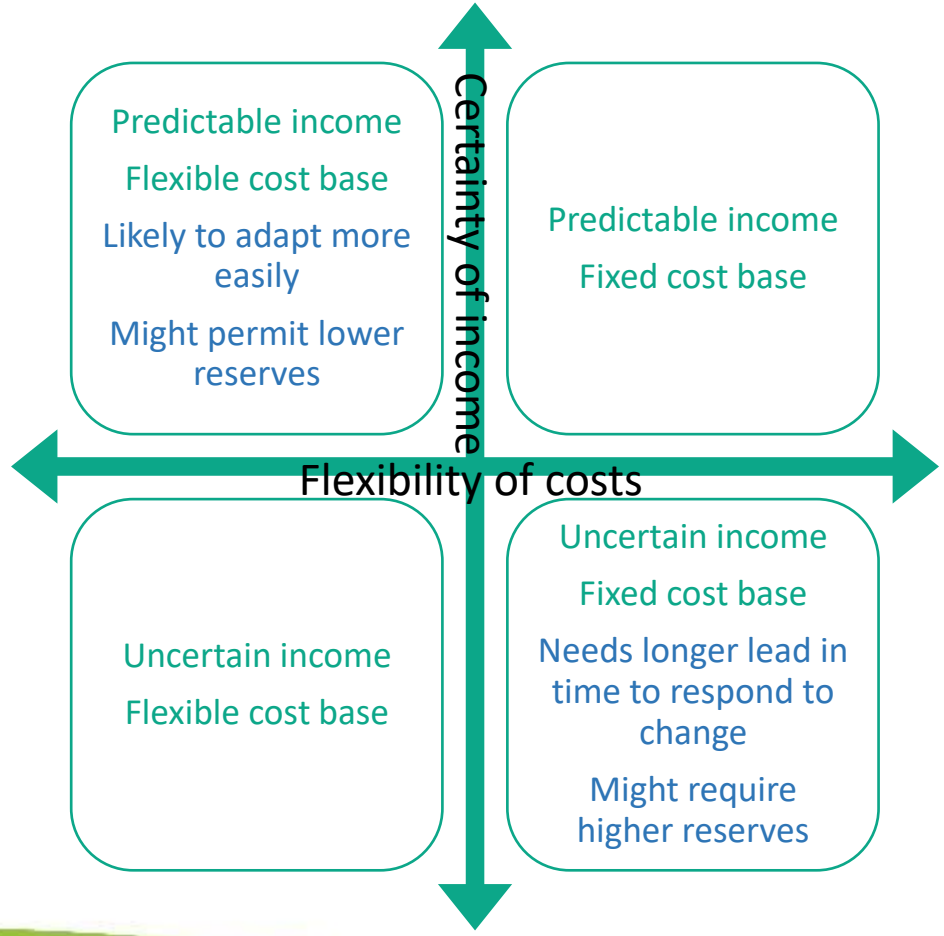
How to calculate a target level



Adapted from ReservesPoliciesMadeSimple-SayerVincent-July2015.pdf

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How to calculate the target level

An example of how we might adopt a risk based approach to identifying a target reserves level.

Redundancy liability	£10k
Legal commitments e.g. rent/leases	£10k
Upcoming repairs to the office	£10k - £20k
Bridging funds between contracts	£10k
Total = Target range of reserves required	£40k - £50k

Developing our reserves policy

Charities are required to state their policy on reserves in their Trustee's Annual Report:

1. Why the charity needs reserves and the target level identified – oftenexpressed as number of month's running costs
2. The level of actual reserves held and how the organisation is working towards the target level
3. How the organisation will keep their policy under review
4. Where the charity does not have a reserves policy in place, it should include a statement to that effect
5. Where funds have been designated, the reserves policy statement should state how much for how long and why
6. There are additional concerns for charities with an income over £500k

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Charity Commission's example reserves policy

Reserves Policy

The Management Committee has examined the charity's requirements for reserves in light of the main risks to the organisation. It has established a policy whereby the unrestricted funds not committed or invested in tangible fixed assets held by the charity should be between 3 and 6 months of the expenditure. Budgeted expenditure for 2009/10 is £550,000 and therefore the target is £137,500 to £275,000 in general funds. The reserves are needed to meet the working capital requirements of the charity and the Management Committee are confident that at this level they would be able to continue the current activities of the charity in the event of a significant drop in funding. Whilst income funds stand at £56,792 a designation of £20,000 has been set aside for the purchase of equipment for the training project and a further £22,500 funds the office equipment of the charity. The present level of reserves available to the charity of £14,292 therefore falls significantly short of this target level. Although the strategy is to continue to build reserves through planned operating surpluses, the Management Committee is well aware that it unlikely that the target range can be reached for at least five years. In the short term the Management Committee has also considered the extent to which existing activities and expenditure could be curtailed, should such circumstances arise.

Other examples are available for different types of charities
Dorsetshire Drugs Advice Centre Example (publishing.service.gov.uk)

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Charity Commission's example reserves policy

Financial review	
Brief statement of the charity's policy on reserves	*Cash at bank at 31/12/2016 was £12k in unrestricted funds. The main financial risk to the charity is loss of funding from the Council and reduced donations. The funds are held to cover 4 months operational costs in the event of a loss of income and to meet any unforeseen expenditure that may occur.*

arwbyc_v2.pdf (publishing.service.gov.uk)

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How to keep reserves under review

Trustees should monitor their actual reserves and keep their policy under review to make sure it is relevant.

We may need to intentionally build up or spend down reserves so that what we hold is in line with our target level.

Low or declining reserves can often be a sign of financial difficulty. Being familiar with the Commission's guidance Managing a charity's finances: planning, managing difficulties and insolvency (CC12) can help us manage this well if and when we need to.

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How to monitor reserves

Often, we leave this until year end when we prepare our year-end accounts.

This can mean that it is sometimes too late to take corrective action in time to avert financial difficulty.

The level of reserves should be monitored throughout the year as part of the normal monitoring and budgetary reporting processes.

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Actual v Budget report
For 1.4.22 - 30.06.22

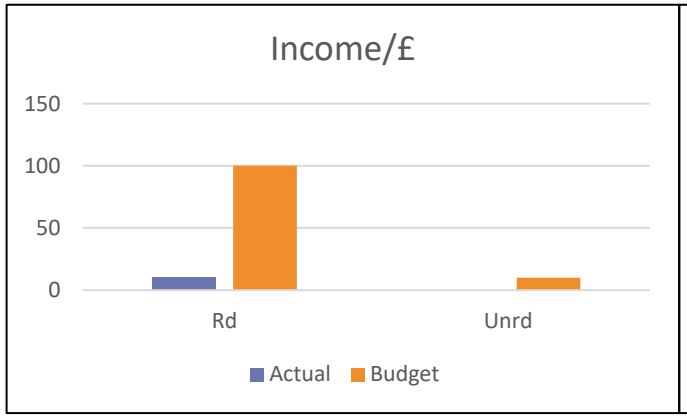
	RESTRICTED												UNRESTRICTED			TOTAL		
	Grant 1			Grant 2			Grant 3			Total			Total					
Income	Actual	Budget	Variance	Actual	Budget	Variance	Actual	Budget	Variance	Actual	Budget	Variance	Actual	Budget	Variance	Actual	Budget	Variance
Total Confirmed grants	10	10	0	0	50	-50	0	10	-10	0	70	-70	0	5	-5	0	75	-75
Total Donations	0	10	-10	0	10	-10	0	10	-10	0	30	-30	0	5	-5	0	35	-35
Total Income	10	20	-10	0	60	-60	0	20	-20	0	100	-100	0	10	-10	0	110	-110
Expenses																		
Total Project costs	0	20	-20	0	0	0	0	30	-30	0	30	-30	0	0	0	0	30	-30
Total Salaries	0	0	0	0	40	-40	0	0	0	0	0	0	0	10	-10	0	10	-10
Total Expenses	0	20	-20	0	40	-40	0	30	-30	0	30	-30	0	10	-10	0	40	-40
Net Income	10	0	10	0	20	-20	0	-10	10	0	70	-70	0	0	0	0	70	-70
Transfers between funds								10			10			-10			0	
Opening balance	100	100		20	20		0	0		120	120		10	10		130	130	
Closing balance	110	100		20	40		0	0		120	200		10	0		130	200	

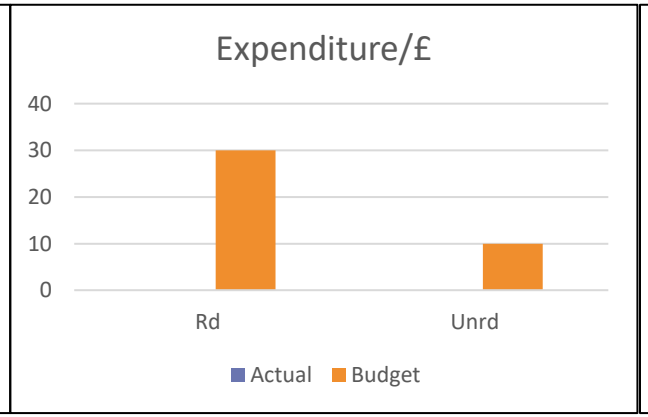
Running costs /m	10
Reserves/m	1
target resere	30

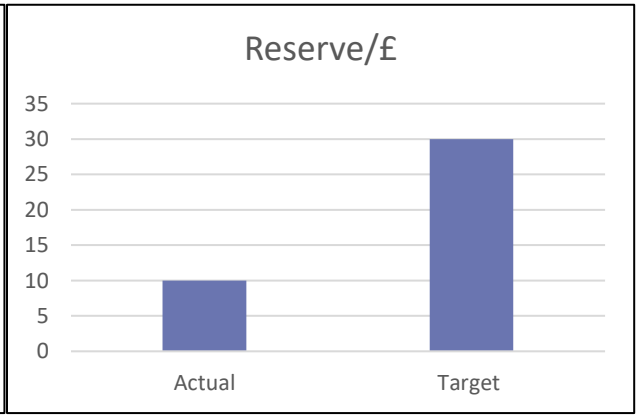
Example monthly finance update

Charity financial position for month 2 of the financial year

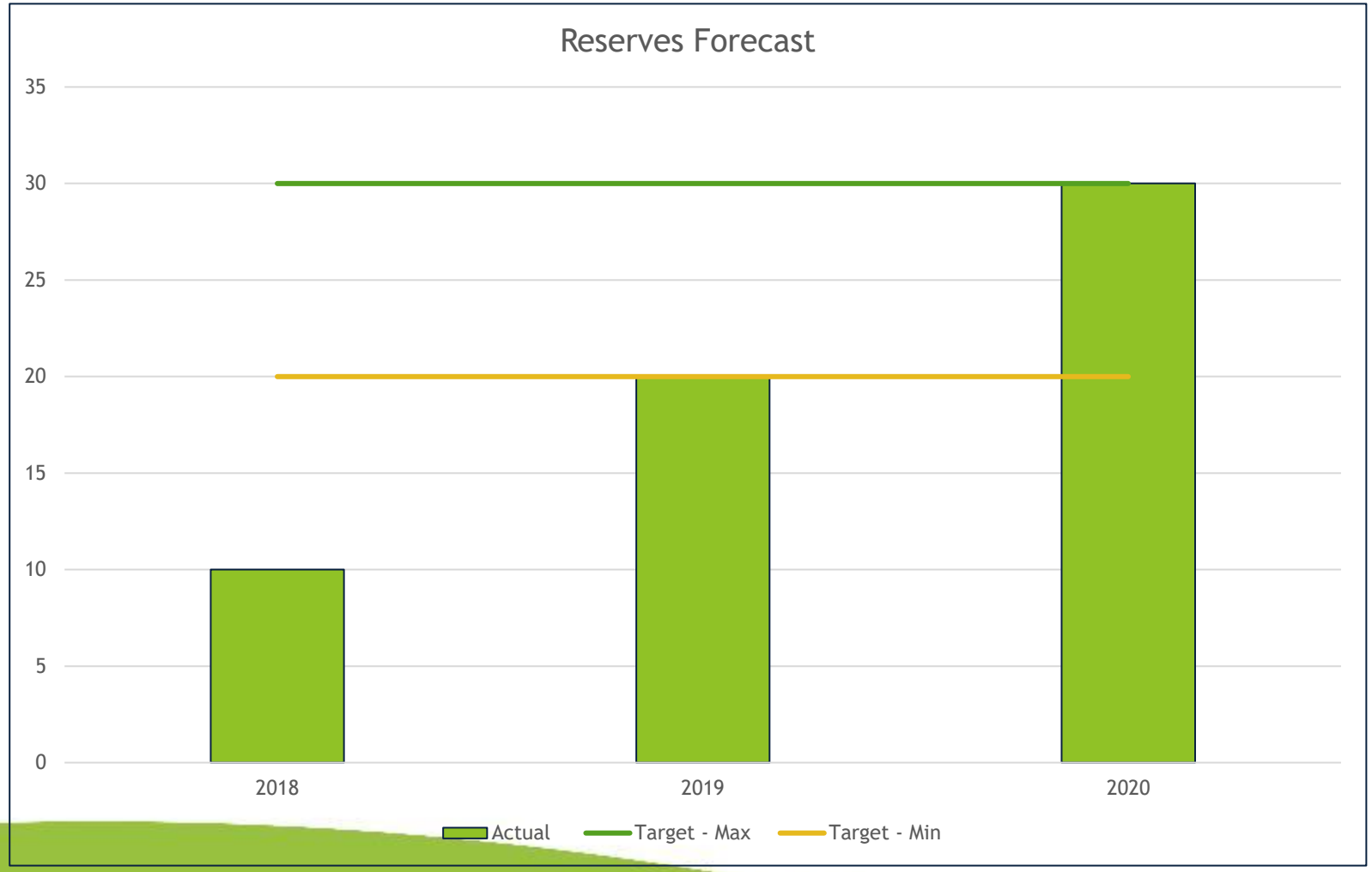
- Restricted income is under budget at £10 received v £100 budgeted. This is due to late receipt of grants. We expect that next month our actual grants received will be in line with our budget expectations set at the beginning of the year.
- Unrestricted income is also under budget. This is because we have not yet had capacity to run the appeal for donations.
- Because the grant income is late, activity on our projects and our core work is yet to begin and so restricted and unrestricted expenditure are under budget. Again, we expect both to be on budget next month.
- Reserves are under budget with £10 compared to the target £30 – largely due to the late appeal.







How to report on reserves mid year



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Inquiry based approach

It can often be difficult to know the answers to finance questions. Our job as leaders is not to have all the answers. It is to ask the right questions and build our team and support network to help us answer the questions together.

Questions we might ask about reserves:

- How much do we have in reserves?
- Have we set a target reserve?
- Have we developed a reserves policy?
- Is it compliant with CC19?
- Do we review the policy?
- Do we monitor reserve levels during the year?

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What is financial resilience?

Financial resilience is the ability to

expand and contract

with integrity and intention

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That takes time – reserves buy us this time

Organizational resilience is the ability of an organization to anticipate, prepare for, respond and adapt to incremental change and sudden disruptions in order to survive and prosper.

Organizational Resilience: A summary of academic evidence, business insights and new thinking BSI (British Standards Institution) and Cranfield School of Management

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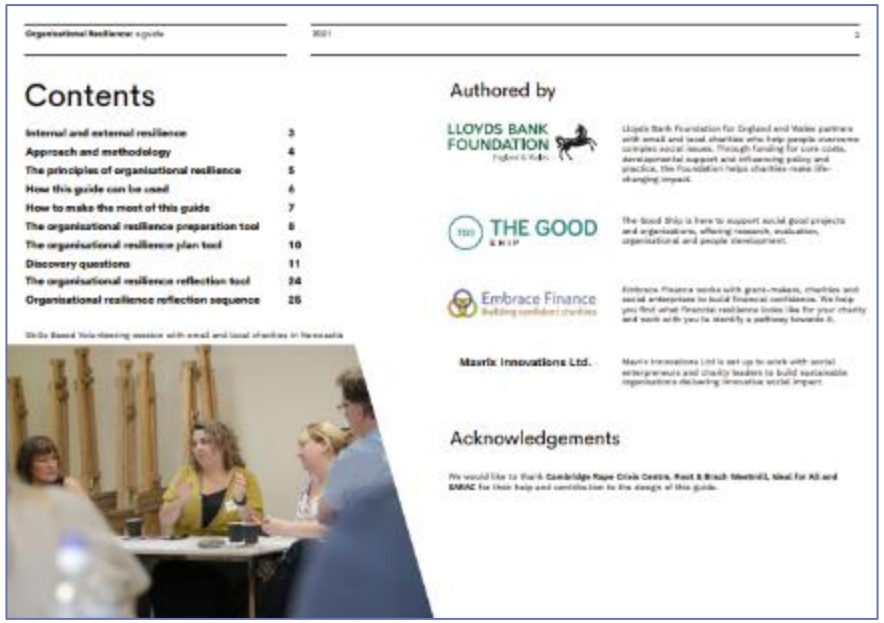
Not sure where to start?



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Authored by

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Mawlx Innovations Ltd.

Acknowledgements

https://www.lloydsbankfoundation.org.uk/we-develop/useful-resources/organisational-resilience-programme

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Not all heroes wear capes, some build resilience charities

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Useful resources

https://www.gov.uk/government/publications/charities-and-reserves-cc19/charities-and-reserves

https://www.embracefinance.org.uk/

https://www.sayervincent.co.uk/publications/reserves-policies-made-simple/

https://www.bond.org.uk/resources/building-financial-reserves-for-resilient-organisations/

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